

ORIGINAL

OPEN MEETING



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MEMORANDUM

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Arizona Corporation Commission

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2006 OCT -3 P 2:06

TO: THE COMMISSION OCT -3 2006

FROM: Utilities Division

DOCKETED BY

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AZ CORP COMMISSION  
DOCUMENT CONTROL

DATE: October 3, 2006

RE: IN THE MATTER OF THE MERGER OF MOUNTAIN  
TELECOMMUNICATIONS, INC. AND ESCHELON TELECOM, INC. FOR  
WAIVER OF RULE 14-2-803 OF THE PUBLIC UTILITY HOLDING COMPANIES  
AND AFFILIATED INTERESTS RULES AND JOINT NOTICE OF INTENT TO  
TRANSFER CONTROL (DOCKET NO T-03432A-06-0451)

Introduction

On July 7, 2006, Mountain Telecommunications, Inc. ("MTI-AZ") and Eschelon Telecom, Inc. ("Eschelon" or "ETI") filed a joint application for waiver of Rule 14-2-803 of the Public Utility Holding Companies and Affiliated Interest Rules and Joint Notice of Intent to Transfer Control in connection with a proposed transaction whereby Eschelon will acquire 100 percent control of MTI-AZ. In the alternative, the Applicants requested that the Commission approve the progress transaction without a hearing.

On July 28, 2006 in Decision 68866, the Commission approved the suspension of the application up to and including November 3, 2006.

Between July 28, 2006 and August 28, 2006, the Applicants provided information to assist Staff in its analysis of the joint application.

On August 16, 2006, MTI-AZ, ETI and Staff discussed associated information needs via a telephone conference.

Background of Applicants

MTI-AZ is an Arizona public service corporation, with its principal place of business in Tempe, Arizona. MTI-AZ is a wholly-owned subsidiary of Mountain Telecom, Inc. ("MTI-DE"), a Delaware corporation.

On February 9, 1998, in Decision No. 60668, the Commission granted a Certificate of Convenience and Necessity ("CC&N") to MTI-AZ, authorizing it to provide facilities-based and resold local exchange and long distance telecommunications services in Arizona.

ETI is a Delaware corporation with its principal place of business in Minneapolis, Minnesota. ETI's wholly-owned subsidiary, Eschelon Telecom of Arizona ("ETI-AZ"), is a

utility certified to provide telecommunications services in Arizona in accordance with Decision No. 62751, dated July 25, 2000.

On April 17, 2002, in Decision 64737, ETI-AZ was granted a limited waiver of the Commission's Affiliated Interest Rules, including A.A.C. R14-2-803, which provided that it shall only be required to comply with that rule for "any proposed organization or reorganization, transaction, or diversification plan that could directly or indirectly result in or cause an increase in its maximum rate on file with the Commission for any competitive service."<sup>1</sup>

On June 29, 2006, the Parties consummated a merger agreement.

On July 6, 2006 the parties filed a Joint Application for Consent to Transfer of Control with the Federal Communications Commission ("FCC"). The FCC approved the Applicants' merger application on August 26, 2006.

#### The Applicants' Transaction

MTI-AZ and ETI in their application represent the following:

1. Pursuant to the Agreement, Mountain Acquisition Corp., a newly created subsidiary of Eschelon Operating Company ("OPCO") will be merged with and into MTI-DE.
2. As a result of the merger, the separate corporate existence of Mountain Acquisition Corp. shall cease and MTI-DE will continue as the surviving corporation of the merger as a wholly owned subsidiary of OPCO, which is a wholly owned subsidiary of ETI. MTI-AZ, an Arizona public service corporation and a wholly-owned subsidiary of MTI-DE will remain a wholly-owned subsidiary of MTI-DE.
3. Upon completion of the transaction, ETI will be the ultimate parent company for MTI-AZ.
4. Upon completion of the proposed transaction, MTI-DE and MTI-AZ will operate in Arizona as wholly-owned subsidiaries of ETI.
5. This transaction will not directly or indirectly result in or cause an increase in the maximum rates on file for MTI-AZ or ETI-AZ.
6. As a part of the transactions, ETI will purchase all of the stock of MTI-DE with cash.
7. After completion of the transaction, the capital structure of MTI-AZ will have the same assets but less debt than before the transaction.

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<sup>1</sup> Decision No. 64737, page 4, lines 21 – 23.

THE COMMISSION

October 3, 2006

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8. The merger will not have a negative impact on the cost of service of MTI-AZ.
9. MTI-AZ will continue to fund a substantial portion of its capital expenditure needs with internally generated funds. The reorganization positions MTI-AZ to take advantage of the financial strength and other resources of ETI for any additional capital needs. To the extent that additional funds are needed, access to funds will likely be more readily available at a lower cost than would be available to the utility under present circumstances.

The Applicants Request

The Applicants seek review and approval of this transaction without a hearing under A.A.C. R14-2-803.

Staff's Analysis and Conclusions

ETI-AZ provides local, long distance and internet services to several thousand business customers primarily in the Phoenix metro area. MTI-AZ also provides services to customers in Tucson metro area and to a limited number of rural areas in the state.

While both ETI-AZ and MTI-AZ have noteworthy presence in facilities-based local exchange service for business customers primarily in the Enterprise Market, neither provider has any significant presence within Residence or the Mass Markets.

MTI-AZ provides central office services to Saddleback Communications but not end-user retail services. With the conclusion of this proposed transaction, ETI-AZ will be assuming responsibility for the services provided by MTI-AZ to Saddleback Communications.

A copy of the customer notice that was mailed to all MTI-AZ customers on September 26, 2006 has been provided to Staff and is included as Attachment A. Additionally, MTI-AZ has conducted fact-to-face discussions with its top 50 customers and expects to conduct similar discussions with all Phoenix and Tucson metro customers by the end of October 2006.

Customer services and agreements will not change as a result of this merger as MTI-AZ and ETI-AZ will continue to operate separately.

The Applicants have indicated to Staff that no merger-related plans to reduce the Arizona employee-base of the joint Applicants' operations exist at this time and have expressed plans to actually increase Eschelon's sales force by 20 employees within one year of merger closing.

Eschelon is in the process of acquiring assets consisting of Tel West customer accounts in Washington state and will be acquiring, in its entirety, OneEighty Communications, a Montana company with operations in Montana and Wyoming. However, Eschelon has indicated that these activities will not impact Arizona operations.

THE COMMISSION

October 3, 2006

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The Parties are not proposing any changes to the respective CC&Ns granted by the Commission to MTI-AZ or ETI-AZ.

The Parties have been found to be in compliance and good standing by the Commission's Compliance and Consumer Services sections.

Staff is not aware of any parties that have raised concerns or filed objections to this transaction.

Staff's Recommendations

Staff recommends that the joint application of MTI-AZ and ETI for review and approval of this transaction without a hearing under A.A.C. R14-2-803 be approved.

Staff further recommends that the Commission order include the following conditions:


1. That for one year following acquisition close or until MTI-AZ and ETI inform the Commission by filing an affidavit with Docket Control that acquisition-related activities are completed, whichever occurs last, MTI-AZ and ETI provide written notification to the Director of the Utilities Division and to the individual members of the Commission, at least 60 days in advance, of any planned acquisition-related Arizona workforce layoffs; any planned acquisition-related Arizona plant closings; and any planned acquisition-related Arizona facility closings.
2. That MTI-AZ and ETI provide Commission Staff, via Protective Agreement, with updates by April 15, 2007 and April 15, 2008 on the status of plans proposed in this Transaction to increase employees and investment in Arizona.
3. That MTI-AZ and ETI provide Commission Staff, via Protective Agreement, with updates by April 15, 2007 and April 15, 2008 of any changes in the status of debt financing plans.
4. That MTI-AZ and ETI be required to review its numbering resources in the 480, 520, 602, 623, and 928 Numbering Plan Areas ("NPA"). To the extent that the Company's numbering resources in these NPAs exceed a six month inventory,

THE COMMISSION

October 3, 2006

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MTI-AZ and ETI be required to, within sixty days of a Commission Decision in this matter, return to the Pooling Administrator all surplus thousands-blocks with less than ten percent contamination and inform the Commission of such actions through a filing in docket control.

for   
Ernest G. Johnson  
Director  
Utilities Division

EGJ:AFF:lhv\JMA

ORIGINATOR: Armando F. Fimbres

August 1, 2006

Dear Valued Customer:

I am writing to share with you an exciting announcement regarding your Mountain Telecommunications, Inc. (MTI) services. Recently, MTI and Eschelon Telecom, Inc. ("Eschelon") signed a definitive agreement whereby Eschelon will acquire MTI. The transaction is expected to be finalized in the fourth quarter of 2006 and is subject to customary regulatory approvals.

Eschelon is a provider of integrated voice, data, Internet services and business telephone systems, that serves over 55,000 customers in eight states. One of the fastest growing telecommunications companies in the nation, Eschelon is proud to be a leader in the industry in customer satisfaction and customer retention. Eschelon has a long-standing commitment to Arizona, having served this state since 2000.

By bringing MTI and Eschelon together, you will benefit from a wider range of expertise and resources. You will continue to be supported by a team of highly-trained associates who will provide best-in-class customer service. In addition, we are pleased to offer the following:

- Broad statewide and national service area to serve your current and future locations
- Comprehensive suite of products to support the voice and data needs of large and small business locations
- Business telephone systems from the industry's leading manufacturers including NEC and Inter-Tel
- Enhanced Internet capabilities including security solutions, 24/7 technical support and Eschelon's comprehensive Service Level Agreement
- E-Billing, Eschelon's free online billing and analysis tool

**What are the next steps?**

There is no need for you to do anything. All existing customer contracts will be honored and supported. We are confident that you will continue to be satisfied with our quality services, and that you will continue to receive the same high level of customer service and support that you have come to expect from us. We will provide you with advance notice on any planned changes in billing statement design, remittance addresses and customer contact information. If you have any questions about this letter, please contact us at the same customer service number, 480-850-9555. Thank you.

Sincerely,

Gina Gallegos  
Director of Customer Relations  
480-850-7523  
Mountain Telecommunications, Inc.

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**BEFORE THE ARIZONA CORPORATION COMMISSION**

JEFF HATCH-MILLER  
Chairman  
WILLIAM A. MUNDELL  
Commissioner  
MIKE GLEASON  
Commissioner  
KRISTIN K. MAYES  
Commissioner  
BARRY WONG  
Commissioner

IN THE MATTER OF THE MERGER OF  
MOUNTAIN TELECOMMUNICATIONS,  
INC. AND ESCHELON TELECOM, INC.  
FOR WAIVER OF RULE 14-2-803 OF THE  
PUBLIC UTILITY HOLDING COMPANIES  
AND AFFILIATED INTERESTS RULES  
AND JOINT NOTICE OF INTENT TO  
TRANSFER CONTROL

DOCKET NO. T-03432A-06-0451  
  
DECISION NO. \_\_\_\_\_  
ORDER

Open Meeting  
October 17 and 18, 2006  
Phoenix, Arizona

BY THE COMMISSION:

Introduction

On July 7, 2006, Mountain Telecommunications, Inc. ("MTI-AZ") and Eschelon Telecom, Inc. ("Eschelon" or "ETI") filed a joint application for waiver of Rule 14-02-803 of the Public Utility Holding Companies and Affiliated Interest Rules and Joint Notice of Intent to Transfer Control in connection with a proposed transaction whereby Eschelon will acquire 100 percent control of MTI-AZ. In the alternative, the Applicants requested that the Commission approve the proposed transaction without a hearing.

On July 28, 2006 in Decision No. 68866, the Commission approved the suspension of the application up to and including November 3, 2006.

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FINDINGS OF FACTBackground of Applicants

1. MTI-AZ is an Arizona public service corporation, with its principal place of business in Tempe, Arizona. MTI-AZ is a wholly-owned subsidiary of Mountain Telecom, Inc. ("MTI-DE"), a Delaware corporation.

2. On February 9, 1998, in Decision No. 60668, the Commission granted a Certificate of Convenience and Necessity ("CC&N") to MTI-AZ, authorizing it to provide facilities-based and resold local exchange and long distance telecommunications services in Arizona.

3. ETI is a Delaware corporation with its principal place of business in Minneapolis, Minnesota. ETI's wholly-owned subsidiary, Eschelon Telecom of Arizona ("ETI-AZ"), is a utility certified to provide telecommunications services in Arizona in accordance with Decision 62751, dated July 25, 2000.

4. On April 17, 2002, in Decision 64737, ETI-AZ was granted a limited waiver of the Commission's Affiliated Interest Rules, including A.A.C. R14-2-803, which provided that it shall only be required to comply with that rule for "any proposed organization or reorganization, transaction, or diversification plan that could directly or indirectly result in or cause an increase in its maximum rate on file with the Commission for any competitive service."<sup>1</sup>

5. On June 29, 2006, the Parties consummated a merger agreement.

6. On July 6, 2006 the Parties filed a Joint Application for Consent to Transfer of Control with the Federal Communications Commission ("FCC").

7. Staff is not aware of any parties that have raised concerns or filed objections to this transaction.

The Applicants' Transaction

8. MTI-AZ and ETI in their application represent the following:

- a. Pursuant to the Agreement, Mountain Acquisition Corp., a newly created subsidiary of Eschelon Operating Company ("OPCO") will be merged with and into MTI-DE.

<sup>1</sup> Decision No. 64737, page 4, lines 21 – 23.



- 1           b. As a result of the merger, the separate corporate existence of Mountain  
2 Acquisition Corp. shall cease and MTI-DE will continue as the surviving  
3 corporation of the merger as a wholly owned subsidiary of OPCO, which is a  
4 wholly owned subsidiary of ETI. MTI-AZ, an Arizona public service  
5 corporation and a wholly-owned subsidiary of MTI-DE will remain a wholly-  
6 owned subsidiary of MTI-DE.
- 7           c. Upon completion of the transaction, ETI will be the ultimate parent company  
8 for MTI-AZ.
- 9           d. Upon completion of the proposed transaction, MTI-DE and MTI-AZ will  
10 operate in Arizona as wholly-owned subsidiaries of ETI.
- 11           e. This transaction will not directly or indirectly result in or cause an increase in  
12 the maximum rates on file for MTI-AZ or ETI-AZ.
- 13           f. As a part of the transactions, ETI will purchase all of the stock of MTI-DE  
14 with cash.
- 15           g. After completion of the transaction, the capital structure of MTI-AZ will have  
16 the same assets but less debt than before the transaction.
- 17           h. The merger will not have a negative impact on the cost of service of MTI-AZ.
- 18           i. MTI-AZ will continue to fund a substantial portion of its capital expenditure  
19 needs with internally generated funds. The reorganization positions MTI-AZ  
20 to take advantage of the financial strength and other resources of ETI for any  
21 additional capital needs. To the extent that additional funds are needed, access  
22 to funds will likely be more readily available at a lower cost than would be  
23 available to the utility under present circumstances.

24 The Applicants Request

25           9. The Applicants seek review and approval of this transaction without a hearing  
26 under A.A.C. R14-2-803.

27 Staff's Analysis and Conclusions

28           10. ETI-AZ provides local, long distance and internet access services to several  
thousand business customers primarily in the Phoenix metro area. MTI-AZ also provides service  
to customers in the Tucson metro area and to a limited number of rural areas in the State.

...

...

1           11.     While both ETI-AZ and MTI-AZ have noteworthy presence in facilities-based local  
2 exchange service for business customers primarily in the Enterprise Market, neither provider has  
3 any significant presence within Residence or the Mass Market.

4           12.     MTI-AZ provides central office services to Saddleback Communications but not  
5 end-user retail services. With the conclusion of this proposed transaction, ETI-AZ will be  
6 assuming responsibility for the services provided by MTI-AZ to Saddleback Communications.

7           13.     A copy of the customer notice that was mailed to all MTI-AZ customers on  
8 September 26, 2006 has been provided to Staff and is included as Attachment A. Additionally,  
9 MTI-AZ has conducted fact-to-face discussions with its top 50 customers and expects to conduct  
10 similar discussions with all Phoenix and Tucson metro customers by the end of October 2006.

11           14.     Customer services and agreements will not change as a result of this merger as  
12 MTI-AZ and ETI-AZ will continue to operate separately.

13           15.     The Applicants have indicated to Staff that no merger-related plans to reduce the  
14 Arizona employee-base of the joint Applicants' operations exist at this time and have expressed  
15 plans to actually increase Eschelon's sales force by 20 employees within one year of merger  
16 closing.

17           16.     Eschelon is in the process of acquiring assets consisting of Tel West customer  
18 accounts in Washington state and will be acquiring, in its entirety, OneEighty Communications, a  
19 Montana company with operations in Montana and Wyoming. However, Eschelon has indicated  
20 that these activities will not impact Arizona operations.

21           17.     The Applicants are not proposing any changes to the respective CC&Ns granted by  
22 the Commission to MTI-AZ or ETI-AZ.

23           18.     The Applicants have been found to be in compliance and good standing by the  
24 Commission's Compliance and Consumer Services sections.

25           19.     The FCC approved the Applicants' merger application on August 26, 2006.

26           20.     Staff recommends that the joint application of MTI-AZ for review and approval of  
27 this transaction without a hearing under A.A.C. R14-2-803 be approved.

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21. Staff further recommends that the Commission order include the following conditions:

1. That for one year following acquisition close or until MTI-AZ and ETI inform the Commission by filing an affidavit with Docket Control that acquisition-related activities are completed, whichever occurs last, MTI-AZ and ETI provide written notification to the Director of the Utilities Division and to the individual members of the Commission, at least 60 days in advance, of any planned acquisition-related Arizona workforce layoffs; any planned acquisition-related Arizona plant closings; and any planned acquisition-related Arizona facility closings.
2. That MTI-AZ and ETI provide Commission Staff, via Protective Agreement, with updates by April 15, 2007 and April 15, 2008 on the status of plans proposed in this Transaction to increase employees and investment in Arizona.
3. That MTI-AZ and ETI provide Commission Staff, via Protective Agreement, with updates by April 15, 2007 and April 15, 2008 of any changes in the status of debt financing plans.
4. That MTI-AZ and ETI be required to review its numbering resources in the 480, 520, 602, 623, and 928 NPAs. To the extent that the Company's numbering resources in these NPAs exceed a six month inventory, MTI-AZ and ETI be required to, within sixty days of a Commission Decision in this matter, return to the Pooling Administrator all surplus thousands-blocks with less than ten percent contamination and inform the Commission of such actions through a filing in docket control.

#### CONCLUSIONS OF LAW

1. MTI-AZ and ETI are public service corporations within the meaning of Article XV of the Arizona Constitution.

2. The Commission has jurisdiction over MTI-AZ and ETI and the subject matter in this filing.

3. The Commission, having reviewed the filing and Staff's Memorandum dated October 3, 2006, concludes that it is in the public interest to approve the proposed transaction whereby ETI will acquire 100 percent control of MTI-AZ, and that no hearing is required.

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ORDER

IT IS THEREFORE ORDERED that the joint application of MTI-AZ and ETI for approval of the proposed transaction whereby ETI will acquire 100 percent control of MTI-AZ is approved.

IT IS FURTHER ORDERED that for one year following acquisition close or until MTI-AZ and ETI inform the Commission by filing an affidavit with Docket Control that acquisition-related activities are completed, whichever occurs first, MTI-AZ and ETI provide written notification to the Director of the Utilities Division and to the individual members of the Commission, at least 60 days in advance, of any planned acquisition-related Arizona workforce layoffs; any planned acquisition-related Arizona plant closings; and any planned acquisition-related Arizona facility closings.

IT IS FURTHER ORDERED that MTI-AZ and ETI provide Commission Staff, via Protective Agreement, with updates by April 15, 2007 and April 15, 2008 on the status of plans proposed in this Transaction to increase employees and investment in Arizona.

IT IS FURTHER ORDERED that MTI-AZ and ETI provide Commission Staff, via Protective Agreement, with updates by April 15, 2007 and April 15, 2008 of any changes in the status of debt financing plans.

IT IS FURTHER ORDERED that MTI-AZ and ETI be required to review their numbering resources in the 480, 520, 602, 623, and 928 Numbering Plan Areas ("NPA"). To the extent that the Company's numbering resources in these NPAs exceed a six month inventory, MTI-AZ and ETI be required to, within sixty days of a Commission Decision in this matter, return to the Pooling Administrator all surplus thousands-blocks with less than ten percent contamination and inform the Commission of such actions through a filing in docket control within 30 days thereafter.

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1 IT IS FURTHER ORDERED that in the event that the MTI-AZ and ETI transaction does  
2 not close, all compliance conditions in this Decision shall not be required.

3 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

4  
5 **BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION**  
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CHAIRMAN

COMMISSIONER

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COMMISSIONER

COMMISSIONER

COMMISSIONER

11  
12 IN WITNESS WHEREOF, I BRIAN C. McNEIL, Executive  
13 Director of the Arizona Corporation Commission, have  
14 hereunto, set my hand and caused the official seal of this  
15 Commission to be affixed at the Capitol, in the City of  
16 Phoenix, this \_\_\_\_\_ day of \_\_\_\_\_, 2006.

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18 \_\_\_\_\_  
BRIAN C. McNEIL  
19 Executive Director

20 DISSENT: \_\_\_\_\_

21  
22 DISSENT: \_\_\_\_\_

23 EGJ:AFF:lhmm/  
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1 SERVICE LIST FOR: Mountain Telecommunications, Inc. and Eschelon Telecom, Inc.  
2 DOCKET NO. T-03432A-06-0451

3 Ms. Catherine A. Murray  
4 Manager, Regulatory Affairs  
5 Eschelon Telecom, Inc.  
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8 Mr. Mike Hazel  
9 Vice President  
10 Mountain Telecommunications, Inc.  
11 1430 West Broadway Road, Suite A200  
12 Tempe, Arizona 85282

13 Mr. Ernest G. Johnson, Esq.  
14 Director, Utilities Division  
15 Arizona Corporation Commission  
16 1200 West Washington Street  
17 Phoenix, Arizona 85007

18 Mr. Christopher Kempley  
19 Chief Counsel, Legal Division  
20 Arizona Corporation Commission  
21 1200 West Washington Street  
22 Phoenix, Arizona 85007  
23  
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Attachment A

August 1, 2006

Dear Valued Customer:

I am writing to share with you an exciting announcement regarding your Mountain Telecommunications, Inc. (MTI) services. Recently, MTI and Eschelon Telecom, Inc. ("Eschelon") signed a definitive agreement whereby Eschelon will acquire MTI. The transaction is expected to be finalized in the fourth quarter of 2006 and is subject to customary regulatory approvals.

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- Business telephone systems from the industry's leading manufacturers including NEC and Inter-Tel
- Enhanced Internet capabilities including security solutions, 24/7 technical support and Eschelon's comprehensive Service Level Agreement
- E-Billing, Eschelon's free online billing and analysis tool

**What are the next steps?**

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Sincerely,

Gina Gallegos  
Director of Customer Relations  
480-850-7523  
Mountain Telecommunications, Inc.